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Message from the Director

On behalf of the University of Kentucky Internal Audit Department (IA), I am pleased to present our fiscal year 2010 annual report. The report is comprised of three sections. The first section includes information about the IA staff and defines the five primary services provided with the intent of adding value and providing reasonable assurance to the UK community. These services offer IA high-quality flexibility when assessing a business activity or department’s condition. One of the services highlighted is the IA Advisory Program which has the goal of offering objective counsel and education to UK through seminars and consultation services.

The second section of the report covers the IA Quality Assurance Program. In FY 2010, three areas of concentration were: (1) compliance with professional standards and assessing the overall effectiveness of IA; (2) use of five measurable metrics; and (3) infrastructure improvements. Our commitment to this endeavor is shown through favorable metric results for feedback, recommendations accepted and productivity.

The report appendix or third section provides summaries of the audits performed in FY 2010. IA is consistently working to improve audit processes and reduce audit cycle time through various technological advancements highlighted in the report.

As in FY 2010, IA plans to increase coverage through collaborative efforts with various partnerships across the University of Kentucky. We will continue to add value through committee involvement, consultations, continuous auditing, training and presentations and specific counsel. It is our privilege to work with the UK community. We sincerely appreciate and thank the Administration for their support.

Joe Reed,
Senior Director Internal Audit
University of Kentucky

FY 2010 - Internal Audit Staff

Back Row: Anastasia Myers-Wilson, Judy Pistilli
Middle Row: Tamara Mundy, Debbie Kern
Front Row: Joseph Reed, Gretchen Wagner, Bruce Arseneau, Martin Anibaba
Karen Michaels (not pictured)

Internal Audit Senior Director
Joseph Reed

Audit Staff
Martin Anibaba- Principal IT Auditor, Information Technology and comprehensive core reviews
Bruce Arseneau- Senior Auditor, Campus comprehensive core review
Karen Michaels- Principal Auditor, Advisory and UK HealthCare consulting
Anastasia Myers-Wilson- Senior Auditor, UK HealthCare comprehensive core review and special projects
Judy Pistilli- Principal Auditor, Campus and UK HealthCare comprehensive core reviews
Gretchen Wagner- Staff Auditor, Follow up review and comprehensive core review team

Support Staff
Debbie Kern- Quality Assurance Risk Coordinator- Audit Function Oversight/Director’s Assistance
Tamara Mundy- Administrative Staff Associate- Internal Audit Business Office

Internal Audit
2333 Alumni Park Plaza
Suite 110
Lexington, KY 40517
859.257.3126 office
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www.uky.edu/Internal Audit/
Internal Audit Services

“Internal Audit assists the University management, administration and the Board of Trustees in the effective discharge of their fiduciary and administrative responsibility by providing independent, objective assurance and consulting services with respect to evaluating risk management, control and governance processes.”

(Internal Audit Charter, 2005)

- **Comprehensive Core Review**: These reviews evaluate the internal control structure for departments and/or processes utilizing the COSO and COBIT framework. This review focuses on existing practices to assess preventative measures for reasonable assurance.

- **Compliance Review**: These reviews examine adherence with applicable laws, regulations and policies. The compliance review is an audit of historical data, thus focusing on previous activity for reasonable assurance.
  - **Continuous Auditing**: This program evaluates compliance of major university business activities. The audit utilizes computer-aided auditing techniques to test policy adherence for activities such as payroll, benefits, cash, inventory, contracts, grants, etc.

- **Investigation**: An investigation or special project involves the examination of improper activities leading to a monetary or physical loss to the University. The role of Internal Audit is to accurately document the event and determine if an audit of the condition is necessary.

- **Advisory Review**: The review is an agreement between Internal Audit and the Client focusing on administrative efficiency and effectiveness for a specific unit or process, concluding with improvement suggestions. Committee participation and workshops/seminars are also categorized in this service area.

- **Information Technology Review**: These reviews evaluate the internal control structure and safeguards over the information technology resources of the University in line with the control objective for information and related technology (COBIT) framework. For the business unit, this is a review of all software applications for system input, output, access controls, recovery plans and security to provide reasonable assurance.
Internal Audit Advisory Program

The program goal is to offer objective counsel and education to the University of Kentucky.

This service is provided through workshops/seminars, consultation services and unit assessments.

**Workshops/Seminars:**
Internal Audit offers workshops and seminars as a proactive means of educating the UK community on common findings identified during audit work.

Workshops are offered through UK’s Human Resources Training Program on a rotating schedule. Management may also request workshops and seminars for large groups. The table shows FY 2010 workshop statistics.

<table>
<thead>
<tr>
<th>Workshop Type</th>
<th>Number of Attendees</th>
<th>Number of workshops offered in 2010</th>
</tr>
</thead>
<tbody>
<tr>
<td>Cash Handling Workshop</td>
<td>111</td>
<td>5</td>
</tr>
<tr>
<td>Fraud Seminar</td>
<td>99</td>
<td>3</td>
</tr>
<tr>
<td>Procard Operations</td>
<td>150</td>
<td>7</td>
</tr>
<tr>
<td>Management Requested Workshops</td>
<td>17</td>
<td>1</td>
</tr>
</tbody>
</table>

**Other Requests for Advisory Services:**
In FY 2010 Internal Audit received 14 total requests for consultation services and numerous inquiries. Although only a few consultation services could be honored, each inquiry was resolved. Internal Audit classifies an inquiry as: (1) *an area of clarification for general duties*, (2) *a request for general guidance*, or (3) *procedural verification for policy adherence*, from any employee within the UK community.

Consultation services focusing on process improvement can be requested by management in the following areas:

- Procard Activities
- Cash Handling
- Payroll Activities
- Reconciliations
- Administrative Manuals
Internal Audit Quality Assurance Program

In FY 2010 the three areas of concentration were Compliance, Metrics and Infrastructure.

Compliance with the Institute of Internal Auditors (IIA) International Professional Practices Framework: According to IIA Standard 1310, “Internal Audit should adopt a process to monitor and assess the overall effectiveness of the quality program. The process should include both internal and external assessments.”

Internal Audit is committed to continuous improvement and has completed the following assessments:

- Self-Study Assessment completed in September 2004
- Readiness Quality Assessment Review completed in April 2007
- Quality Assessment Review completed in August 2009

Metrics (Internal Audit Scorecard): The UK Internal Audit department measures itself utilizing metrics on a quarterly and annual basis:

- Metric #1: 75% Productivity Rate
- Metric #2: 110% of Forecast Hours vs. Actual Hours
- Metric #3: 75% Acceptance Rate for Recommendations
- Metric #4: 3.0 Rating for Client Satisfaction
- Metric #5: 100% Work Plan Completion Rate

Infrastructure Improvements: UK Internal Audit is consistently working to improve audit processes and reduce audit cycle time. The technological advancements listed below have been purchased or developed in FY 2010 to enhance overall efficiency and effectiveness. Implementation and execution are the present challenges for these advancements.

- Audit Universe: A database of all units and processes that aids in the risk assessment process.
- Auto Audit: An audit management and documentation tool.
- ACL: A software program utilized for conducting continuous auditing and monitoring.

“All of our expectations have changed since the University of Kentucky Internal Audit was formed in 1958, from wanting a value-added Internal Audit function at UK to requiring one. “Quality Assurance” is one way Internal Audit achieves this goal, along with continued support and collaboration.” (Joseph Reed, Internal Audit Senior Director)
METRIC #1: PRODUCTIVITY
Departmental Goal of 75% Productivity

A productivity goal of 75% translates to actual hours of production. The hours are calculated from the total amount of work hours per professional employee (2080 hours) multiplied by 75% to compute the total available hours for Audit Projects. FY 2010 productivity exceeded this goal with an actual rate of 82%. This calculation is used to forecast individual audit assignments for the annual work plan. Actual hours in FY 2010 are shown below. The table represents a breakdown of Audit Project Hours and Non-Audit Project Hours.

### 2010 Productivity Rate

- **Audit Project Hours**: 9,277 hours (82%)
- **Non-Audit Project Hours**: 1,959 hours (18%)

### Audit Project Hours

These categories represent the cumulative number of hours that were charged to each service area. The percentages show actual time spent in each service area to Total Audit Project Hours.

<table>
<thead>
<tr>
<th>Service Area</th>
<th>Hours</th>
<th>Percentage</th>
</tr>
</thead>
<tbody>
<tr>
<td>Core Review</td>
<td>4,403</td>
<td>47%</td>
</tr>
<tr>
<td>Infrastructure</td>
<td>1,437</td>
<td>16%</td>
</tr>
<tr>
<td>Follow-Up</td>
<td>1,282</td>
<td>14%</td>
</tr>
<tr>
<td>Compliance</td>
<td>840</td>
<td>9%</td>
</tr>
<tr>
<td>Advisory</td>
<td>782</td>
<td>8%</td>
</tr>
<tr>
<td>Information Systems</td>
<td>304</td>
<td>3%</td>
</tr>
<tr>
<td>Investigations</td>
<td>229</td>
<td>3%</td>
</tr>
<tr>
<td><strong>Total</strong></td>
<td><strong>9,277</strong></td>
<td><strong>100%</strong></td>
</tr>
</tbody>
</table>

### Non-Audit Project Hours

These categories represent the cumulative number of hours that were charged to each area for non-project time. The percentages show actual time spent in each area to Total Non-Audit Project Hours.

<table>
<thead>
<tr>
<th>Service Area</th>
<th>Hours</th>
<th>Percentage</th>
</tr>
</thead>
<tbody>
<tr>
<td>Approved Leave Time</td>
<td>690</td>
<td>35%</td>
</tr>
<tr>
<td>General Administration</td>
<td>553</td>
<td>28%</td>
</tr>
<tr>
<td>Training</td>
<td>445</td>
<td>23%</td>
</tr>
<tr>
<td>Staff Meeting</td>
<td>271</td>
<td>14%</td>
</tr>
<tr>
<td><strong>Total</strong></td>
<td><strong>1,959</strong></td>
<td><strong>100%</strong></td>
</tr>
</tbody>
</table>
METRIC #2: PLANNED VS. ACTUAL HOURS

Departmental Goal of 110% of Planned Hours

This metric is calculated by using forecasted hours by service area versus actual hours to be in an acceptable range for each work plan assignment. In FY 2010 the focus on infrastructure continuous improvements and major business activities for follow-up audits increased actual project hours in these service areas.

<table>
<thead>
<tr>
<th>Service Area</th>
<th>Planned Hours</th>
<th>Actual Hours</th>
<th>Percentage</th>
</tr>
</thead>
<tbody>
<tr>
<td>Infrastructure</td>
<td>1,000</td>
<td>1,437</td>
<td>144%</td>
</tr>
<tr>
<td>Follow Up</td>
<td>580</td>
<td>1,282</td>
<td>221%</td>
</tr>
<tr>
<td>Advisory</td>
<td>1,200</td>
<td>782</td>
<td>65%</td>
</tr>
<tr>
<td>Core</td>
<td>4,500</td>
<td>4,403</td>
<td>98%</td>
</tr>
<tr>
<td>Compliance</td>
<td>1,480</td>
<td>840</td>
<td>57%</td>
</tr>
<tr>
<td>Information Systems</td>
<td>300</td>
<td>304</td>
<td>101%</td>
</tr>
<tr>
<td>Investigations</td>
<td>300</td>
<td>229</td>
<td>76%</td>
</tr>
<tr>
<td><strong>Total</strong></td>
<td><strong>9,360</strong></td>
<td><strong>9,277</strong></td>
<td><strong>99%</strong></td>
</tr>
</tbody>
</table>

The chart below shows forecasted hours against actual hours for several audits completed in the FY 2010 Work Plan. The major business activity focus and information systems inclusion have increased hours for many assignments.
This chart compliments Metric #2 with all Advisories, Special Projects and Audit Requests that were not part of the initial FY 2010 Work Plan. The 1,095 unallocated hours were used as follows:

### Actual Hours for Unplanned Audits 2010

<table>
<thead>
<tr>
<th>Project Description</th>
<th>Actual Hours</th>
</tr>
</thead>
<tbody>
<tr>
<td>2010IR02 CAER</td>
<td>38</td>
</tr>
<tr>
<td>2010IR01 PIMSER</td>
<td>189</td>
</tr>
<tr>
<td>2010MCR02 Outreach Center for Science</td>
<td>91</td>
</tr>
<tr>
<td>2010A100 Procard Separation of Duties</td>
<td>61</td>
</tr>
<tr>
<td>2010A08 UK Surplus Auction</td>
<td>104</td>
</tr>
<tr>
<td>2010A06 Physical Medicine and Rehab: Cash</td>
<td>9</td>
</tr>
<tr>
<td>2010A05 Commercialization and Economic</td>
<td>31</td>
</tr>
<tr>
<td>2010A04 CNS: Procard Review</td>
<td>172</td>
</tr>
<tr>
<td>2010A03 Radiology</td>
<td>333</td>
</tr>
<tr>
<td>2010A02 Lockbox Inventory</td>
<td>13</td>
</tr>
<tr>
<td>2010A01 KMSF</td>
<td>54</td>
</tr>
</tbody>
</table>

### AUDIT DURATION

This chart compliments Metric #2 by showing the average number of Business days and Audit hours to complete a review by each service area. An increased focus on major business activities and information systems have improved effectiveness, but caused some inefficiency. Internal Audit infrastructure enhancements discussed in the Quality Assurance Program section on page 5 are being implemented to address these concerns.

### Audit Duration 2010

<table>
<thead>
<tr>
<th>Category</th>
<th>Average Hours per Audit</th>
<th>Average Days per Audit</th>
</tr>
</thead>
<tbody>
<tr>
<td>Advisory Reviews</td>
<td>114</td>
<td>51</td>
</tr>
<tr>
<td>Core Reviews</td>
<td>116</td>
<td>101</td>
</tr>
<tr>
<td>Compliance Reviews</td>
<td>239</td>
<td>255</td>
</tr>
<tr>
<td>Follow Up Reviews</td>
<td>255</td>
<td>110</td>
</tr>
</tbody>
</table>
METRIC #3: RECOMMENDATIONS ACCEPTED
Departmental Goal of 75 % Accepted Recommendations

Recommendations are categorized as those that are accepted, those that are not accepted, and those that do not require a management response. Internal Audit's goal is to have 3 out of every 4 recommendations requiring a response from management to be accepted. The goal was achieved, as 100% of the recommendations requiring a response from management were accepted.

“Internal Audit will furnish management with analyses, recommendations, counsel and information concerning the activities examined.” (IA Charter, 2005)

AUDITOR TRAINING

* IA Professional Audit Staff (qualifications below) received 445 Hours of Training in 2010 *

![Auditor Qualifications Chart]

2010 Training Provided by:

- Central Kentucky Institute of Internal Auditors (CKIIA)
- Institute of Internal Auditors (IIA)
- College Business Management Institute
- American College and University Auditors (ACUA)
- SAP/IRIS Training
- UK Human Resources Training
- ExecuTrain of Kentucky
- Internal Audit-UK
METRIC #4: COMMUNICATION

Departmental Goal of 3.0 for Client Satisfaction - Rating Scale of 1.0 - 4.0

The three areas of concentration are Survey Results, Communication Activities and Partnerships.

FY 2010 Survey Results: Client feedback is focused in 3 areas: Professionalism, Communication and Value. Internal Audit's cumulative rating was well above satisfactory for clients who submitted feedback using the following rating scale: 1.0 – Not Satisfied; 2.0 – Somewhat satisfied; 3.0 – Satisfied; 4.0 – Very Satisfied. The feedback we receive is vital in helping us improve our services and structure additional services to benefit the entire UK community.

Communication Activities: (Newsletters & Website)

Internal Audit publishes quarterly newsletters for the University community. We use the newsletters as a means of communicating current trends at the University and hot topics in the auditing profession. Internal Audit is continually looking for ways to communicate with our clients to ensure working with our team is a pleasant learning experience. Please take a look at our website (www.uky.edu/Internal_Audit/) which is being updated to meet UK’s needs.

Partnerships across the University:

- College of Medicine
- General Counsel
- Human Resources
- Information Technology
- Office of the Treasurer
- Provost Office
- UK HealthCare
- UK Police

"Great discoveries and improvements invariably involve the cooperation of many minds.”
Alexander Graham Bell
METRIC #5: WORK PLAN COMPLETION RATE

Departmental Goal of 100% Completion

This table is the FY 2010 Amended Work Plan by service area as approved by the Audit Subcommittee in March 2010.

<table>
<thead>
<tr>
<th>Service Area</th>
<th>Planned</th>
<th>Completed</th>
<th>Percentage</th>
</tr>
</thead>
<tbody>
<tr>
<td>Infrastructure</td>
<td>3</td>
<td>3</td>
<td>100%</td>
</tr>
<tr>
<td>Advisory</td>
<td>9</td>
<td>9</td>
<td>100%</td>
</tr>
<tr>
<td>Campus Core</td>
<td>3</td>
<td>1</td>
<td>33%</td>
</tr>
<tr>
<td>UK HealthCare Core</td>
<td>5</td>
<td>3</td>
<td>60%</td>
</tr>
<tr>
<td>Information Systems</td>
<td>1</td>
<td>0</td>
<td>0%</td>
</tr>
<tr>
<td>Compliance</td>
<td>7</td>
<td>4</td>
<td>57%</td>
</tr>
<tr>
<td>Special Projects</td>
<td>2</td>
<td>2</td>
<td>100%</td>
</tr>
<tr>
<td><strong>Total</strong></td>
<td><strong>30</strong></td>
<td><strong>22</strong></td>
<td><strong>73%</strong></td>
</tr>
</tbody>
</table>

- Infrastructure assignments focused on technological advances.
- Advisory activities focused on procard, cash handling and payroll procedures.
- Campus Core reviews focused on business unit processes.
- UK HealthCare Core reviews focused on functional activities and business unit processes.
- Information Systems focused on security and application controls.
- Compliance reviews focused on centralized business activities across UK.
- Special Projects focused on adherence to UK policies and procedures associated with specific events.

EXECUTIVE AUDIT PROJECT HOURS

The total project hours (9,277) are allocated across Executive area through a number of factors including management request, unforeseen event, regulatory commitment, or risk assessment. The objective is to perform enough relevant work to make a knowledgeable annual assessment for possible trends or concerns.

<table>
<thead>
<tr>
<th>Executive Area</th>
<th>2010 Hours</th>
</tr>
</thead>
<tbody>
<tr>
<td>Provost</td>
<td>2,806</td>
</tr>
<tr>
<td>HealthCare</td>
<td>3,985</td>
</tr>
<tr>
<td>Finance &amp; Administration</td>
<td>2,486</td>
</tr>
</tbody>
</table>
CORE REVIEWS

C02 College of Education: Collaborative Center for Literacy Development
The purpose of this audit was to provide reasonable assurance that effective controls are in place at the senior-administrative level of the Collaborative Center for Literacy Development (CCLD). This was to ensure that UK’s objectives are being met as they relate to the reliability and integrity of financial reporting and the safeguarding of assets, and that the CCLD is in compliance with applicable laws and regulations. Internal Audit expressed ‘Observations’ in areas of business processes and information systems that required management’s attention. Our office made 14 recommendations, all of which management accepted.

MC01 Department of Orthopedic Surgery and Sports Medicine
The purpose of this audit was to provide reasonable assurance that effective controls are in place at the senior administrative level of the Department of Orthopedic Surgery and Sports Medicine (Ortho). This was to ensure UK’s attainment of objectives are reported with reliability and integrity through financial reporting on operations, that university assets are properly safeguarded, and that Ortho is in compliance with applicable laws and regulations. Internal Audit reviewed internal controls and IT objectives based on the COBIT model. Our office made 10 recommendations, and management accepted all of them.

MCR01 Department of Obstetrics and Gynecology
The purpose of this audit was to provide reasonable assurance that effective controls are in place at the senior administrative level of Obstetrics and Gynecology (OB/GYN). This was to ensure that UK’s objectives are being met as they relate to the reliability and integrity of financial reporting, that university assets are properly safeguarded, and that OB/GYN is in compliance with applicable laws and regulations. The review indicated adequate cash controls at ancillary locations and centralized disbursement controls under OB/GYN’s purview are operating effectively. Audit results, expressed as “Observations,” indicate that the following items require management’s attention: revenue management utilization and human resources protocol. Internal Audit made two recommendations and management accepted both.

MCR02 Outreach Center for Science
The purpose of this audit was to provide reasonable assurance to UK senior management regarding compliance activities and the integrity and reliability of the financial reporting by the Outreach Center for Science (OCS) as it relates to OCS’s three accounts: Operating, Gift and Internet Grant Writing Program. Internal Audit results indicate effective controls are implemented around the revenue processes. Our office made two recommendations to management, both of which management accepted.

ADVISORY: Consultations and Inquiries

The 2010 fiscal year represented the second full year of consultation services offered by Internal Audit. Consultations result in an informal report issued to a department/unit’s management. Our office performed seven consultations in FY 2010. Of the seven advisory consultations, the following were areas requested for reviews: Three on cash handling, three on Procard, two on unit assessment, and one on payroll.
COMPLIANCE REVIEWS

CST01 MCPPD Work Orders
The purpose of this audit was to review work orders of the Medical Center Physical Plant Division (MCPPD). Internal Audit focused on work order descriptions, revisions and charges and the associated invoices created by MCPPD for clients. Internal Audit issued a management letter documenting concerns and related recommendations to address the concerns.

CST02 MCPPD Tools Management
The purpose of this audit was to review the tools management processes at MCPPD. Internal Audit focused on compliance with tool internal policies, issuance of tools to employees and safeguarding of tools. Internal Audit presented the findings to management and discussed associated concerns and recommendations.

CST03 Center for Rural Health
The purpose of this audit is an annual review of the Center for Rural Health (CRH) for fiscal year 2010 as mandated by KRS 164.937. This audit of CRH primarily focused on financial performance, adherence to UK’s Business Procedures Manual, and compliance of grant activity. CRH grants were administered properly and in accordance with sponsor specifications. Internal Audit made two recommendations, which management accepted.

CST300 DAV
The purpose of this auditing project was a review of the centralized Department Authorization and Voucher (DAV) documents located at Accounts Payable. The results were consistent with the 2006 Accounts Payable review showing adequate payment timeliness and duplicate payment results.

SPECIAL PROJECTS
There were two special projects conducted by Internal Audit that focused on adherence to UK policies and procedures associated with specific events. These results found compliance concerns, but no improper activities. No reports were issued due to the work performed by Internal Audit.

FOLLOW UP
Internal Audit planned five follow-up reviews for this fiscal year. The follow-up reviews assess the findings issued in the original report. The chart below represents the results of the follow-up reviews.

<table>
<thead>
<tr>
<th>Audit</th>
<th>Number of Original Recommendations</th>
<th>Follow-Up Results</th>
</tr>
</thead>
<tbody>
<tr>
<td>FR01 Orthopedics</td>
<td>4 Recommendations</td>
<td>3 Fully Addressed 1 Not Addressed</td>
</tr>
<tr>
<td>FR02 Center for Rural Health</td>
<td>3 Recommendations</td>
<td>2 Fully Addressed 1 Partially Addressed</td>
</tr>
<tr>
<td>FR03 Microbiology</td>
<td>6 Recommendations</td>
<td>3 Fully Addressed 2 Partially Addressed 1 Pending</td>
</tr>
<tr>
<td>FR04 Accounts Payable</td>
<td>2 Recommendations</td>
<td>2 Fully Addressed</td>
</tr>
<tr>
<td>FR07 Kentucky Clinic South</td>
<td>4 Recommendations</td>
<td>1 Fully Addressed 1 Partially Addressed 2 Not Addressed</td>
</tr>
</tbody>
</table>